STATE OF MICHIGAN
IN THE SUPREME COURT

Appeal from the Court of Appeals
(Murphy, C.J., and O'Connell and Beckering, JJ.)

WAYNE COUNTY EMPLOYEES RETIREMENT SYSTEM and WAYNE COUNTY RETIREMENT COMMISSION,

Plaintiffs-Counterdefendants-Appellees,

v

CHARTER COUNTY OF WAYNE,

Defendant-Counterplaintiff-Appellant,

and

WAYNE COUNTY BOARD OF COMMISSIONERS,

Defendant-Appellant.

Docket No. 147296

Court of Appeals No. 308096

Wayne County Circuit Court
LC No. 10-013013-AW
Hon. Michael F. Sapala

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# DEFENDANTS-APPELLANTS WAYNE COUNTY AND WAYNE COUNTY BOARD OF COMMISSIONERS' BRIEF ON APPEAL

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## BASIS OF JURISDICTION

On September 29, 2011, the Wayne County Circuit Court issued its "Opinion and Order of the Court Granting Defendant Wayne County's Motion for Summary Disposition." (App 274a). The Wayne County Employees Retirement System and the Wayne County Retirement Commission filed a claim of appeal to the Michigan Court of Appeals, which reversed the trial court's decision in a published opinion issued on May 9, 2013. (App 278a). On April 1, 2014, this Court granted the application for leave to appeal filed by Defendants-Appellants Wayne County and Wayne County Board of Commissioners ("Wayne County"). (App 319a).

## STATEMENT OF QUESTIONS INVOLVED

In granting leave to appeal in this case, the Court directed the parties to address the following three issues (which, as seen below, are supplemented with two additional issues):

(1) "An identification of the source and nature of the County's power to move funds from the Inflation Equity Fund (IEF)."

The trial court did not explicitly address this issue.

The Court of Appeals did not explicitly address this issue.

| | |
|---|---|
| Wayne County answers: | The Michigan Constitution, the Charter Counties Act, and Wayne County's charter provide the County with this power. |

This issue also implicates the Court of Appeals' suggestion that moving funds from the IEF may violate Const 1963, art 9, § 24, which prohibits "accrued financial benefits" from being diminished or impaired, an issue on which the Court had previously requested briefing. A similar protection is provided in both the Charter Counties Act and Wayne County's charter. Wayne County will thus address the following issue in conjunction with its answer to the Court's issue (1): Whether the 2010 ordinance violates art 9, § 24 of the Michigan Constitution.

| | |
|---|---|
| The trial court would answer: | No. |
| The Court of Appeals would answer: | No as to individual retirees, but there arguably may be a "group entitlement." |
| Wayne County answers: | No. |

(2) "Whether the movement of IEF assets to the defined benefit plan without the corresponding offset to the County's Annual Required Contribution violates the Public Employee Retirement System Investment Act (PERSIA), MCL 38.1132 *et seq*."

The trial court did not address this issue, but presumably would answer no.

The Court of Appeals would answer: Yes.

Wayne County answers: No.

Since issue (2) relates only to the theoretical transfer of IEF assets to the defined benefit plans *without* a corresponding offset to Wayne County's ARC, whereas the 2010 ordinance explicitly provides for such an offset, Wayne County will also address the following issue: Whether the movement of IEF assets to the defined benefit plan *with the corresponding offset* to the County's ARC violates PERSIA.

The trial court would answer: No.

The Court of Appeals would answer: Yes.

Wayne County answers: No.

(3) "Whether the movement of $32 million in IEF assets to the defined benefit plan constitutes a 'transaction' within the meaning of MCL 38.1133(6)?"

The trial court would answer: No.

The Court of Appeals would answer: Yes.

Wayne County answers: No.

## I. INTRODUCTION

Wayne County established the Wayne County Retirement System ("the Retirement System") in 1944. The Retirement System generally consists of five defined benefit plans, one defined contribution plan, and the "Inflation Equity Fund" ("IEF"). Wayne County created the IEF in 1986 by ordinance, which authorized the Retirement Commission to establish an IEF effective November 30, 1985, and to fund it using assets from the defined benefit plans. In 1986, the Retirement Commission transferred funds from the defined benefit plans to the IEF for years 1985 and 1986. Since then, the IEF has continued to be funded by additional transfers from the defined benefit plans, and has been used to give retirees an extra "bonus" check (known as a "13th check") above and beyond their accrued retirement benefits. In 2010, a Wayne County ordinance resulted in IEF funds being transferred back into the defined benefit plans from which those funds originally came. These transfers were all between funds *within* the Retirement System, never *left* the Retirement System, and the transferred funds are to be used exclusively to pay retiree benefits.

Notwithstanding those undisputed facts, the Court of Appeals held that the 2010 ordinance: (1) violated the Public Employee Retirement System Investment Act's ("PERSIA") "exclusive benefit" rule, MCL 38.1133(6) (providing that "the assets of the system shall be for the exclusive benefit of the participants and their beneficiaries"),[1] because the transfer had the effect of reducing the amount of Wayne County's "annual required contribution" (ARC) to the defined benefit plans; and (2) violated PERSIA's "prohibited transaction" rule, MCL 38.1133(6)(c) (prohibiting, in relevant part, "[a] transfer to, or use by or for the benefit of, the

[1] MCL 38.1133(6) is now MCL 38.1133(8).

political subdivision sponsoring the system of any assets of the system for less than adequate consideration"). The Court of Appeals was simply wrong and should be reversed.

The Michigan Constitution and law authorize Wayne County, through the Wayne County Board of Commissioners, to pass local laws to deal with local concerns. Unless those laws violate the Michigan Constitution or statute, courts may not invalidate them. Yet the Court of Appeals could hardly mask its disdain for Wayne County's Enrolled Ordinance 2010-514 (the "2010 ordinance"), which transferred $32 million out of the Retirement System's IEF and returned it to the Retirement System's defined benefit plans.[2]

The Court of Appeals accused Wayne County of "invad[ing] the assets of the IEF to lessen its financial burden," and concluded that "the shift of IEF funds to the defined benefit plan totally ignored the prior controlling versions of the IEF ordinance and the intent manifested therein." But Wayne County properly exercised its legislative authority in enacting the 2010 ordinance and did not violate either the Michigan Constitution or any law.

In granting Wayne County's application for leave to appeal, this Court ordered the following issues to be briefed:

> (1) an identification of the source and nature of the County's power to move funds from the Inflation Equity Fund (IEF); (2) whether the movement of IEF assets to the defined benefit plan without the corresponding offset to the County's Annual Required Contribution violates the Public Employees Retirement System Investment Act (PERSIA), MCL 38.1132 et seq.; and (3) whether the movement of $32 million in IEF assets to the defined benefit plan constitutes a "transaction" within the meaning of MCL 38.1133(8).

The first issue is simple. The Michigan Constitution authorizes counties to adopt charters and local laws and permits the Michigan Legislature to prescribe a charter county's authority. The Michigan Charter Counties Act (the "CCA"), MCL 45.501 *et seq.*, requires charter counties

[2] The $32 million resulted in a one-time partial offset to Wayne County's 2010-2011 ARC to the defined benefit plans.

to include certain provisions in their charters, including provisions for continuing existing retirement systems and modifying those systems. The Home Rule Charter for the County of Wayne, in turn, allows Wayne County to modify the Wayne County Retirement System, which includes the IEF. Pursuant to that constitutional and statutory authority, Wayne County simply modified the Retirement System when it enacted the 2010 ordinance.

The CCA and Wayne County's charter also include provisions that mirror the Michigan Constitution's protection of retirement system accrued financial benefits. This Court made clear in *Studier v Mich Pub Sch Employees' Retirement Bd*, 472 Mich 642; 698 NW2d 350 (2005), and *In re Request for Advisory Opinion Regarding Constitutionality of 2011 PA 38*, 490 Mich 295; 806 NW2d 683 (2011), that "accrued financial benefits" are financial benefits that both (1) increase or grow over time, and (2) can be funded "in the year that service was rendered." 13th checks meet neither of those requirements because the discretionary decision whether to distribute a 13th check to a particular person in a given year is made only after the employee retires. Thus, 13th checks are nothing like regular retirement benefits that accumulate and grow during an employee's working years and can be funded each year on account of the employee's services that year. Because 13th checks are not "accrued financial benefits," the 2010 ordinance does not violate art 9, § 24 or the similar CCA and Wayne County charter provisions.

Second, the Court asked Wayne County to address whether the transfer of IEF funds back into the defined benefit plans would violate PERSIA *if there were no corresponding offset to Wayne County's ARC*. Because transferring IEF funds back into the defined benefit plans would increase the amount of assets in the defined benefit plans, it would cause the County's ARC to be re-calculated and reduced. Thus, *with or without an explicit ARC offset*, Wayne County's ARC would be reduced by transferring IEF assets back into the defined benefit plans. Under either scenario, the PERSIA analysis is the same – because Retirement System assets exclusively go to pay benefits to participants and their beneficiaries, the Court of Appeals plainly erred in finding a violation of PERSIA's "exclusive benefit" and "prohibited transaction" rules.

The Court of Appeals first held that the 2010 ordinance violates PERSIA's "exclusive benefit" rule, MCL 38.1133(6) (now MCL 38.1133(8)), a conclusion based on its erroneous belief that the assets of the *discretionary* IEF, which was derived from the defined benefit plans in the first instance, could only be used to issue discretionary 13th checks and cannot be returned to the defined benefit plans for the payment of accrued benefits. That misbelief permeated the Court of Appeals' exclusive benefit rule analysis and its conclusion that Wayne County impermissibly "benefited" when IEF assets were moved back into the defined benefit plans as a partial offset to the County's ARC for fiscal year 2010-2011. However, the Court of Appeals failed to consider that MCL 38.1133(6) only requires that the assets of the *retirement system as a whole* be used for the "exclusive benefit" of participants and beneficiaries, and does not prohibit an *intra-system transfer* of retirement system assets. With or without an offset to its ARC, the 2010 ordinance does not cause Wayne County to "use" retirement system "assets" for its own "benefit" within the meaning of MCL 38.1133(6) because those assets were never used, and they are not being used, for any purpose other than to pay benefits to Retirement System participants and their beneficiaries.[3]

The Court of Appeals further held – and this implicates the Court's third question – that the intra-system movement of IEF assets back into the defined benefit plans also constituted a

[3] As discussed further below, federal courts applying ERISA have found similar intra-system transfers and offsets to not violate ERISA's exclusive benefit rule. See *Holliday v Xerox Corp*, 732 F2d 548, 551 (CA 6, 1984) (holding that transfer of funds from one pension account to another, and subsequent use of transferred funds as a setoff in calculating retirement benefits, was permissible under ERISA).

"transaction" prohibited by MCL 38.1133(6)(c), which prohibits the "transfer to, or use by or for the benefit of, the political subdivision sponsoring the system of any assets of the system for less than adequate consideration" This too was error. MCL 38.1133(6) only prohibits certain "transactions" between a "retirement system" and either "a party in interest" or "the political subdivision sponsoring the system." On its face, the statute does not apply to purely *intra-system* asset transfers of the kind involved here. Moreover, transferring IEF assets back into the defined benefit plans (again, with or without the corresponding offset to the County's ARC) did not involve either a transfer of assets "to" the system sponsor or use of assets "by" or "for the benefit" of the system sponsor. No assets left the Retirement System or were otherwise "used" for anything other than paying retirement benefits.

## II. <u>FACTUAL AND PROCEDURAL BACKGROUND</u>

### A. Wayne County's Retirement System and IEF

The Retirement System was established in 1944 and is made up of five defined benefit plans, one defined contribution plan, and the IEF. (COA Op (*Wayne County Employees Retirement System v Charter County of Wayne*, 301 Mich App 1; 836 NW2d 279 (2013)), at 12-13, App 287-288a).

The defined benefit plans' assets are used to pay the twelve monthly checks to which all eligible retirees and beneficiaries are entitled. (See *id.* at 6, App 284-285a). In contrast, the IEF provides for discretionary bonus checks, known as "13th checks," to eligible retirees – from excess investment earnings generated during economic boom times. (*Id.*). The IEF is governed by § 141-32 of the Wayne County Code of Ordinances, as amended by the 2010 ordinance.[4]

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[4] Although the IEF is considered to be a separate fund, it is merely one of several accounting "reserves" within the Retirement System. IEF assets are not actually kept in a separate account. (See § 141-37 of the Retirement Ordinance, App 340a (stating that "[t]he descriptions of the

Footnote continued on next page ...

The defined benefit plans are funded by employer contributions from Wayne County and by investment returns (see Plaintiffs' Answer, ¶ 13, App 26a). On the other hand, Wayne County established the IEF in 1986 by ordinance, which authorized the Retirement Commission to establish an IEF effective November 30, 1985. (See Pre-Amendment Chart's Ex 1-A, Enrolled Ordinance 86-284, App 95a). In 1986, the Retirement Commission transferred funds from the defined benefit plans to the IEF for years 1985 and 1986. (See Wayne County Retirement System Inflation Equity Adjustment (13th Month Checks) for the years 1985-1986, App 171a).

Over the years, the IEF has been maintained by additional transfers from the defined benefit plans. (See *id.* for the years 1985-2009, App 171-176a). Transfers from the defined benefit plans to the IEF are authorized when the rate of investment return in any given year is above a "threshold" rate that the Retirement Commission sets, in which case the Retirement Commission, subject to its fiduciary duties, may choose to transfer the "excess" investment returns to the IEF. (See Retirement Ordinance 141-32, App 338a). The Retirement Commission, in turn, invests the defined benefit plans' assets together with the funds maintained in the IEF account. (Preliminary Injunction 12/10/10 Transcript, 49:13-50:13, App 208-209a). Although it invests the funds together, the Retirement Commission holds the defined benefit plans accountable for any investment losses, but holds the IEF harmless from those losses. (See Ps' Resp to Ds' First Set of Discovery, Requests for Admission Nos. 1 and 2, App 214-215a) ("Plaintiffs/Counter-Defendants admit that the IEF does not share in investment losses of the Retirement System.").

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reserve accounts shall be interpreted to refer to the accounting records of the retirement system and not to the segregation of assets by reserve account")).

## B. The Discretionary 13th Checks Distributed From the IEF

All eligible retirees and beneficiaries of the defined benefit plans are *entitled to* twelve monthly checks each year from the defined benefit plans' assets (see 5/11/11 Deposition of Robert Grden, 60:22-62:17, and Annual Actuarial Valuation Report, 2009, App 112-113a and 124-125a). In addition to the twelve annual checks to which they are entitled, some retirees and beneficiaries may also receive a discretionary bonus 13th check from the IEF.[5]

Since the IEF was established, the Retirement Commission has had discretion to distribute 13th checks. *Wayne County*, 301 Mich App at 14-15, App 288-289a.[6] The discretionary 13th check distributions made from the IEF *are not earned for service in the year in which service is actually rendered.* Moreover, the method that the Retirement Commission has used to determine 13th check amounts has varied over the years.[7]

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[5] Despite Plaintiffs' repeated suggestion that 13th checks are something other than purely discretionary payments, the record reflects otherwise. (See CBA Chart, App 236-240a) (illustrating twenty collective bargaining agreements addressing eligibility for 13th checks); Ds' Resp to Ps' First Set of Discovery Requests, Requests for Admissions Nos. 55-58, App 231-233a (addressing eligibility language in four CBAs); Pre-Amendment Chart, App 93-94a (showing discretionary distribution language contained in all prior versions of § 141-32); 5/27/11 Deposition of Judith Kermans, 26:17-27:5, App 117a; 5/11/11 Deposition of Robert Grden, 31:9-20, App 109a).

[6] While the Court of Appeals suggested that the IEF was originally intended to replace cost-of-living adjustments (COLAs), that is completely irrelevant and does not change the fact that 13th checks have always been discretionary. See *Green Oak Twp v Munzel*, 255 Mich App 235, 240; 661 NW2d 243 (2003) (explaining that courts may not speculate about the probable intent of a legislative body beyond the language expressed in the statute or ordinance). Moreover, times and circumstances change, and non-contractual legislative enactments generally cannot bind subsequent legislatures. *Studier v Mich Pub School Employees' Retirement Bd*, 472 Mich 642, 668; 698 NW2d 350 (2005).

[7] See 2005 13th Check Amounts Final Results, 2007 13th Check Amounts Final Results (Revised), 2008 13th Check Amounts Final Results, and Wayne County Retirement System Inflation Equity Adjustment (13th Checks) for the years 1985-2007 and 1996-2009 (showing the average 13th check for 2004 at $2,380, for 2005 at $2,361, for 2006 at $2,030, for 2007 at

Footnote continued on next page ...

Regardless of the method, each year the IEF funds that the Retirement Commission makes available for 13th checks are broken down into a unit value based upon the number of "eligible persons." (See, e.g., 2005 13th Check Amounts Final Results, App 126a). The unit value is then multiplied by the number of units each "eligible person" has, which is based upon the number of years an "eligible person" has been retired and the number of years an "eligible person" worked, subject to a maximum. (6/2/11 Deposition of Ronald Yee, 62:13-63:16, App 181a; 2005 13th Check Amounts, App 126a).

Over the years, the Retirement Commission has repeatedly voted to reduce 13th check amounts depending on the value of retirees' guaranteed monthly payments from the defined benefit plans.[8] In addition, the Retirement Commission has always had discretion to restrict issuing 13th checks depending on the effective date of a retiree's pension. (See Pre-Amendment Charts, App 93-94a).

### C. Wayne County's 2010 Ordinance Transferring Funds From the Retirement System's IEF to the Retirement System's Defined Benefit Plans

On September 30, 2010, the Wayne Board adopted the 2010 ordinance, which, among other things, amended Wayne County Ordinance § 141-32 to change how the IEF is maintained and administered. (See Wayne County Enrolled Ordinance No. 2010-514, App 226-228a). Section 141-32 now states:

Footnote continued from previous page ...

$1,686 and for 2008 at $1,703) (App 126-176a). See also 5/27/11 Deposition of Judith Kermans, 105:10-108:6, App 118-119a).

[8] See 10/1/10 Retirement Commission Meeting Minutes, WCRC000338, App 187a) (Mr. Hutting moved to reduce 13th check amounts by 25% for pensions over $50,000, 50% for pensions over $75,000 and 65% for pensions over $100,000); 9/29/09 Retirement Commission Meeting Minutes, WCRC000352, App 192a (Mr. Grden moved to reduce 13th check amounts by 90% for retirees with pensions over $100,000); 7/15/11 Deposition of Augustus Hutting, 48:23-50:7, App 199-200a (providing that the Retirement Commission has the authority to reduce 13th checks based on pension value); 6/2/11 Deposition of Ronald Yee, 73:18-74:12, App 182-183a (same).

(a) The retirement commission shall maintain a reserve for inflation equity provided that the fund shall be limited to no more than $12,000,000.

(b) (1) Subject to the limit of (a) above, the retirement commission may credit the reserve at the end of each fiscal year with a portion of the excess, if any, of the rate of return on the actuarial value of retirement system defined benefit assets over the rate established for this purpose by the retirement commission.

(2) The retirement commission shall establish the portion of the reserve fund available for distribution to retired members and survivor beneficiaries; provided that portion shall not exceed $5,000,000.00.

(3) The calculation of "defined benefit assets" shall exclude the county's retirement contribution for that fiscal year as set forth in section 141-36 provided the amount in the reserve fund in excess of the limit set forth in subsection (a) above shall be debited from the reserve fund and credited to the defined benefit plan assets and such credit shall offset and/or reduce the county's defined benefit contribution requirement and thereafter be considered defined benefit plan assets.

(c) The retirement commission may restrict the distribution and/or the minimum permanent pension to retired members and survivor beneficiaries having a pension effective date prior to dates selected from time to time by the retirement commission.

(d) The formula for the distribution shall be as from time to time determined by the retirement commission and shall take into account the period of retirement and period of credited service.

(e) Nothing in this section shall preclude the county from reducing or eliminating its contribution for a fiscal year in which defined benefit assets exceed defined benefit liabilities.

(f) Within nine months of first annual distribution from this fund, the CFO shall explore and report to the county commission whether it is advantageous to issue bonds as a strategy to fully fund the retirement system and reimburse the inflation equity fund of $32,000,000.00. [Wayne County Code of Ordinances § 141-32, App 334a.]

The 2010 ordinance did not eliminate the IEF's discretionary bonus program, but altered it in two significant ways:

1. The IEF can hold no more than a total of $12 million and distribute no more than $5 million annually.

2. Any amount in the IEF in excess of $12 million must be debited from the IEF and credited as an offset against the County's annual contribution to the Defined Benefit Plans. (See § 141-32(a), (b), and (c)).

**D. Plaintiffs' Lawsuit to Invalidate the 2010 Ordinance**

Soon after the Wayne Board enacted the 2010 ordinance, the Retirement Commission and the Retirement System sued to challenge it. (See First Amended and Restated Complaint for Writ of Mandamus, Declaratory Judgment and Injunctive Relief, App 2-22a). Plaintiffs claimed that transferring IEF funds back into the defined benefit plans (1) violated MCL 38.1140m, which Plaintiffs alleged places any offsets of the County's annual required contribution within the Retirement Commission's sole discretion, and (2) diminished or impaired paying 13th checks in violation of Const 1963, art 9, § 24. (*Id.* at ¶¶ 17-18, App 5-6a). Plaintiffs asked the trial court to repeal the 2010 ordinance in its entirety and to reinstate §§ 141-32 and 141-36. (*Id.* at ¶¶ 72-73, App 12a).

On August 1, 2011, after discovery closed, Wayne County moved for summary disposition on all of Plaintiffs' claims. (See Wayne County's Motion for Summary Disposition Dismissing Plaintiffs' Complaint (filed Aug 1, 2011), App 62-85a). As to Plaintiffs' claim under Const 1963, art 9, § 24, Wayne County identified several bases for concluding that 13th check payments are discretionary and not accrued financial benefits, and that art 9, § 24 therefore did not apply:

*First*, there are no collective bargaining agreements that entitle any person to receive a 13th check. Instead, some CBAs only provide that *if* 13th checks are issued, then certain union members are eligible to receive them. (See, e.g., CBA Chart, App 236-240a (highlighting which

CBAs out of the approximately 20 CBAs produced in this case actually address 13th checks, excluding supporting exhibits)[9]).

*Second*, Plaintiffs admitted that the 13th checks have historically varied in amount each year. (See, e.g., Ps' Resp to Ds' First Set of Discovery, Requests for Admissions No. 22, App 221-222a).

*Third*, the Retirement Commission itself, as recently as 2003, rejected a claim by retirees that benefits payable from the IEF were "accrued financial benefits." (See 6/30/03 Retirement Commission Meeting Minutes, WCRC000495, App 244a).[10]

*Fourth*, Plaintiffs admitted that 13th checks are entirely discretionary. (See 12/10/10 Preliminary Injunction Transcript, 65:11-22, App 210a). Augustus Hutting, a Retirement Commission Trustee since 1991, admitted that 13th checks were always discretionary and did not need to be paid out yearly, even prior to the 2000 amendment. (See 7/15/11 Deposition of Augustus Hutting, 8:15-17; 6:2-4; 13:14-18 and 14:13-18, App 198-198a).

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[9] The CBA Chart was originally attached to Wayne County's Motion for Summary Disposition Dismissing Plaintiff's Complaint and it included copies of each of the 20 CBAs referenced in the exhibit. Since the relevant language of each CBA is pasted into and included in the CBA Chart, the CBAs themselves are not included in the appendix.

[10] The issue arose after the IEF ordinance was amended in 2000 to delete a requirement that if 13th checks were issued in a given year they must account for at least 20%, and no more than 50%, of the IEF. When certain retirees challenged the amendment before the Retirement Commission, the Retirement Commission rejected their claim that 13th checks were accrued financial benefits. (*Id.*) In fact, it was the Retirement Commission that requested the 2000 amendment, and it even participated in the drafting process. (See 6/2/11 Deposition of Ronald Yee, 41:13-42:17, App 179-180a; GRS&C 6/16/2000 Letter, App 251-252a, WCRC001030-001031 (regarding § 26.01(c)); Retirement System 6/30/00 Letter, App 255a, 270-271a, WCRC001009 & 001024-001025 (regarding § 141-32(c)); 6/23/11 Deposition of Richard Noelke, 26:1-15, App 249a (agreeing that the 2000 amendment was initiated by the Retirement Commission)).

*Fifth*, the decision whether to distribute 13th checks, including the amounts of the distributions, is made only *after* an employee has been retired for at least one year. As a result, they do not convey a benefit earned during the year that the benefit was given, so art 9, § 24, simply does not apply to these discretionary bonus checks.

As to Plaintiffs' claim that the credit and offset provisions in the 2010 ordinance conflicted with MCL 38.1140m, Wayne County argued that the statute did not apply because it only applied to offsets using defined benefit plan assets, whereas the Retirement Commission has always treated IEF assets as separate and distinct from defined benefit plan assets, and thus outside the purview of MCL 38.1140m. (See Defendants' Motion for Summary Disposition Dismissing Plaintiffs' Complaint (August 1, 2011), p 13, App 78a). Plaintiffs have repeatedly admitted that IEF assets are not included in the actuarial calculation of the County's annual contribution to the defined benefit plans. (*Id.*)[11] Moreover, the Retirement Commission holds the IEF's assets harmless from investment losses, and allocates those losses solely to the defined benefit plans. (*Id.*)[12] And whereas the defined benefit plan assets are used to pay monthly retirement benefits, the Retirement Commission uses IEF assets to distribute the discretionary 13th checks. (*Id.*)

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[11] See also Preliminary Injunction Transcript, 46:15-19 (Racine), App 207a; Ps' Resp to Ds' First Set of Discovery, Requests for Admissions Nos. 14, 15 and 28, App 218-219a, 223a.

[12] See also Ps' Resp to Ds' First Set of Discovery, Requests for Admission Nos. 1 & 2, App 214-215a ("Plaintiffs/Counter-Defendants admit that the IEF does not share in the investment losses of the Retirement System.").

Finally, Wayne County addressed Plaintiffs' arguments that the 2010 ordinance violated the "exclusive benefit rule" and the prohibited transaction rule. (*Id.* at 14-17, App 79-82a).[13] Although much of Wayne County's argument was based on case law,[14] two key facts demonstrated that the 2010 ordinance did not violate either the exclusive benefit or prohibited transaction rules. First, the 2010 ordinance transferred no assets out of the Retirement System, and thus the assets "will continue to be used by and for the benefit of the Retirement System." (*Id.* at 16, App 81a). Second, the credit and offset provision in MCL 38.1140m permitted the same kind of credit and offset provision created by the 2010 ordinance. (*Id.* at 17, App 82a). Thus, Wayne County argued, because Plaintiffs did not claim the credit and offset provisions of MCL 38.1140m were unlawful, and in fact relied upon them, the substantially similar credit and offset provisions in the 2010 ordinance also did not violate the exclusive benefit rule or the prohibited transaction rule. (*Id.*).

Plaintiffs filed their own motion for summary disposition, to which Wayne County timely responded.

### E. The Trial Court's Decision To Uphold the 2010 Ordinance

On September 7, 2011, the trial court heard the parties' cross-motions for summary disposition. (See 9/29/11 Opinion and Order, App 275a). On September 29, 2011, it issued its "Opinion and Order of the Court Granting Defendant Wayne County's Motion for Summary Disposition." (*Id.*, App 274-277a). The court held that "there are two main issues that compel

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[13] Because Plaintiffs' prohibited transaction rule claim was primarily based upon the prohibited transaction rule found in Internal Revenue Code § 503(b), Wayne County's argument in its summary disposition briefing specifically addressed that provision. (*Id.* at 16-17, App 81-82a).

[14] That case law, including a decision from the United States Supreme Court addressing ERISA's nearly identical exclusive benefit rule, is discussed in detail below.

the result in this case." (*Id.* at 3, App 276a). "The first is whether the IEF is an accrued financial benefit and the second is whether the offset violates MCL 38.1140m." (*Id.*)

The trial court said the plain language of § 141-32 is discretionary and does not create a contractual relationship, and that the relevant collective bargaining agreements "also do not mandate that the payment be made." (*Id.*) The trial court based its ruling on the undisputed evidence that Wayne County submitted:

> Defendant provided the deposition testimony of Augustus Hutting, a Retirement Commission Trustee since 1991. Mr. Hutting testified that the Commission was not required to pay the 13th check. However, if the 13th check was paid, the Commission had to pay out between 20 and 50 percent in order to comply with the ordinance. Furthermore, in order for a contractual right to exist, a legislative act must clearly intend to create a contractual right. Based on the evidence submitted by the parties, the court agrees that the ordinance makes the payment discretionary.
>
> Moreover, the court agrees with Defendant that although the collective bargaining agreements referenced eligibility for the 13th check payment, none of the agreements require or mandate the payment of the 13th check. An "eligible" retiree is qualified to receive a benefit if one is paid, but is not entitled to receive a benefit. The 13th checks are not earned for service in the year rendered. [*Id.* at 3-4, App 276-277a.]

Having found that "the IEF is not an accrued financial benefit," the trial court concluded that the credit and offset provisions of the 2010 ordinance do not violate Const 1963, art 9, § 24. (*Id.* at 4, App 277a).

With regard to Plaintiffs' claim that the offset violates MCL 38.1140m, the trial court summarized Wayne County's argument as follows:

> Defendant argues that the IEF funds may be used to partially offset the County's contribution to the Defined Benefit Plans and that Ordinance 2010-514 does not violate MCL 38.1140m. Defendant maintains that the IEF assets do not constitute assets of the Defined Benefit Plans and that Plaintiffs have admitted that the IEF assets are not included in the actuarial calculation of the County's annual contribution. Defendant further argues that MCL 38.1140m does not address or prohibit the sources from which the annual contribution may be funded, other

> than stating that defined benefit plan assets may not be used to fund the contribution unless the plan is overfunded. [*Id.*]

The trial court observed that Plaintiffs' position essentially was that the statute "does not permit the County to declare certain monies as surplus or excess and therefore subject to offset. Moreover, even if the Retirement System was more than fully funded, the statute provides that there may be an offset and the County cannot assess an offset unless the System consents." (*Id.*) The trial court again agreed with Wayne County, holding that "MCL 38.1140m does not address or prohibit the transfer of funds from the IEF reserve to meet the County's Annual Retirement Contribution Obligation. Therefore, Defendant is entitled to summary disposition on this issue." (*Id.*)

Finally, the trial court summarily rejected Plaintiffs' remaining claims that transferring funds from the IEF to the defined benefit plans violated the "exclusive benefit rule" and constituted a prohibited transaction. (*Id.*) In short, the court "agree[d] with the arguments set for in [Wayne County's] brief on these issues and [found] that the other claims raised in the Complaint and also in Plaintiffs' brief [were] without merit." (*Id.*).

### F. The Court of Appeals' Published Opinion Reversing the Trial Court's Decision

In the Court of Appeals, Plaintiffs again primarily focused on the arguments (1) that the 2010 ordinance impaired accrued financial benefits in violation of art 9, § 24, and (2) that the credit and offset in the 2010 ordinance violated MCL 38.1140m. But the Court of Appeals' opinion paid little heed to those arguments, conceding that "payment of a 13th check ***cannot be viewed as an accrued financial benefit,*** where there is no vested or enforceable right to a 13th check given the discretionary distribution language that has always been part of the IEF ordinance, along with the lack of any CBA language requiring disbursement of a 13th check." (*Wayne County*, 301 Mich App at 34, App 298-299a) (emphasis added). The Court of Appeals also found that the credit and offset did not violate MCL 38.1140m. See *id.* at 52, App 307a ("[W]e have not invalidated the offset pursuant to MCL 38.1140m . . . .") and 54, App 308a ("MCL 38.1140m appears to only address ARCs relative to defined benefit plans . . . .").

The Court of Appeals nonetheless strained to invalidate the 2010 ordinance's credit and offset provisions based on its own analysis of the so-called "plain language" of PERSIA's "exclusive benefit rule" and "prohibited transaction rule," both of which the Court of Appeals found were violated. (*Id.* at 30-46, App 296-304a (exclusive benefit rule), 46-48, App 304-305a (prohibited transaction rule)).[15] As to the "exclusive benefit rule," the Court of Appeals concluded that although no assets were ever removed from the Retirement System, and instead were merely transferred to the defined benefit plans for the exclusive purpose of paying retirement benefits, the County nevertheless received a "benefit" because its ARC was reduced. *Id.* at 35, App 299a ("Instead of honoring and protecting the IEF in connection with its designed purpose, the County Board improperly invaded the assets of the IEF to lessen its financial burden with respect to the ARC.").

Regarding the "prohibited transaction rule," the Court of Appeals concluded that moving funds from the IEF to the defined benefit plans was a "transaction" that "effectively" resulted in both a "transfer" of assets to Wayne County and a "use" of those assets "by or for the benefit of" the County in violation of MCL 38.1133(6)(c). *Id.* at 47-48, App 304-305a ("We conclude that, in violation of MCL 38.1133(6)(c), the 2010 ordinance effectively forced the Retirement Commission to knowingly cause the Retirement System to engage in a transaction that directly

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[15] Wayne County submits that the Court of Appeals' flawed analysis was the product of its contradictory view that although not actually protected by the constitution, "the 13th Check program itself could arguably be viewed as an accrued financial benefit." *Wayne County*, 301 Mich App at 35 n 23, App 299a. As further discussed below, the Court of Appeals' faulty analysis directly conflicts with this Court's precedents.

or indirectly permitted or authorized the County to use or benefit from the use of assets in the IEF absent any consideration. . . . [W]e conclude that it was a sham transaction involving, *effectively*, an unlawful transfer of assets to the County for use to satisfy obligations relative to the ARC.").

Finally, the Court of Appeals found several other provisions of the 2010 ordinance to be invalid, at least in part. The Court of Appeals summarized its holding with respect to those other provisions as follows:

> [W]e invalidate and strike down those provisions in the 2010 ordinance, as codified in WCCO, §§ 141-32 and 141-36, regarding the transfer or reallocation of IEF assets, the offset, the amortization caps and ARC formula, the potential reimbursement of the $32 million IEF excess, and the County's control over an offset decision relative to true defined benefit plan surpluses. The net effect of our ruling is that the excess IEF assets amounting to approximately $32 million must be debited from the defined benefit plan assets and allocated or credited back to the IEF in the accounting records, with the County being left responsible to comply with its ARC obligations absent consideration of the $32 million offset. We, however, also hold that the remaining provisions in the 2010 ordinance are sound and remain intact, including the IEF funding and disbursement caps, as prospectively limited. [COA Op at 41-42, App 302a.]

On November 27, 2013, this Court directed the Court Clerk to schedule oral argument on Wayne County's application for leave to appeal, and ordered the parties to submit supplemental briefs addressing the following questions:

> (1) Whether the Court of Appeals erred in holding that provisions of Wayne County Enrolled Ordinance 2010-514 [(the "2010 ordinance")] violate the Public Employee Retirement System Investment Act, MCL 38.1132 et seq. [("PERSIA")]; and
>
> (2) Whether the ordinance violates Const 1963, art 9, § 24.

After hearing oral arguments on March 5, 2014, the Court granted Wayne County's application for leave to appeal on April 1, 2014.

## III. <u>SUMMARY OF ARGUMENT</u>

Wayne County lawfully amended its retirement ordinance in 2010 based on the authority of the Michigan Constitution, the CCA, and Wayne County's charter. Contrary to Plaintiffs' claim and the Court of Appeals' suggestion, transferring assets from the IEF back into the retirement system's defined benefit plans did not violate Const 1963 art 9, § 24 (or the similar language contained in the CCA and Wayne County's charter) because 13th checks are not "accrued financial benefits." As this Court made clear in *Studier* and *In re Advisory Opinion*, accrued financial benefits "increase or grow over time," whereas 13th checks are discretionary and, even if distributed in a given year to certain retirees, their amounts fluctuate from year to year. Article 9, § 24 also provides that accrued financial benefits are those that arise "on account of service rendered in each fiscal year," which means that the benefit must be one that is capable of being "fund[ed] . . . in the year that the service was rendered." *In re Advisory Opinion*, 490 Mich at 315. 13th checks are not funded in the year the service was rendered, because the decision whether to issue a 13th check to a particular retiree in a given year is not made *until after that person retires*. Accordingly, the 2010 ordinance does not impair accrued financial benefits.

Nor did transferring IEF assets back to the defined benefit plans violate PERSIA's "exclusive benefit" rule, with or without the corresponding offset to the County's ARC. Reducing Wayne County's ARC (whether by its partial offset as provided in the 2010 ordinance or by its recalculation and reduction in the event that IEF assets were simply added to the defined benefit plans) is not the type of "benefit" that is prohibited by PERSIA. All that MCL 38.1133(6) requires is that Retirement System assets not be shared with others. Because IEF assets are not being used for any purpose other than to pay benefits to retirement system participants and their beneficiaries, transferring them back to the defined benefits plans did not violate the "exclusive benefit" rule.

Finally, returning IEF funds back to the defined benefit plans was not a "prohibited transaction." Indeed, this was not a "transaction" *at all* within the meaning of MCL 38.1133(6) because it was a purely *intra-system* transfer of assets, whereas the statute's plain language requires a "transaction" between the Retirement System and *another party*. Nor can moving funds from the IEF back to the defined benefit plans be deemed a transfer "to" or use "by" or "for the benefit" of Wayne County in violation of subsection (c), as the Court of Appeals incorrectly found. No assets left the Retirement System or were otherwise "used" for anything other than paying retirement benefits.

## IV. ARGUMENT

### A. Standard of Review and Controlling Statutory Interpretation Principles

This appeal primarily concerns the proper interpretation of PERSIA's "exclusive benefit" (MCL 38.1133(6)) and "prohibited transaction" (MCL 38.1133(6)(c)) provisions, which presents a question of law that this Court reviews de novo. *Potter v McLeary*, 484 Mich 397, 410; 774 NW2d 1 (2009). In *People v Lowe*, 484 Mich 718, 721-722; 773 NW2d 1 (2009), the Court reiterated the controlling principles governing the interpretation of a statute:

> The Court's responsibility in interpreting a statute is to determine and give effect to the Legislature's intent. The statute's words are the most reliable indicator of the Legislature's intent and should be interpreted based on their ordinary meaning and the context within which they are used in the statute. Once the Court discerns the Legislature's intent, no further judicial construction is required or permitted "because the Legislature is presumed to have intended the meaning it plainly expressed." [Citations omitted.]

"These traditional principles of statutory construction . . . force courts to respect the constitutional role of the Legislature as a policy-making branch of government and constrain the judiciary from encroaching on this dedicated sphere of constitutional responsibility." *People v McIntire*, 461 Mich 147, 153; 599 NW2d 102 (1999).

### B. RESPONSE TO ISSUE #1: The Michigan Constitution, the Charter Counties Act, and Wayne County's charter authorize Wayne County to amend its retirement ordinance to move the IEF funds back into the defined benefit plans.

The Court's order granting leave to appeal asked Wayne County to identify the "source and nature of the County's power to move funds from the [IEF]." The short answer is that it is the same power that the County used to create the IEF within the Retirement System in the first place. As discussed further below, the Michigan Constitution, the CCA, and the Wayne County Charter collectively authorize Wayne County to both implement a retirement system for its employees and to make necessary modifications to it, subject of course to any constitutional or statutory limitations, such as those contained in Const 1963 art 9, § 24 and PERSIA. Wayne County's retirement system is embodied in the Wayne County Retirement Ordinance. Just as Wayne County amended the retirement ordinance in 1986 when it initially established the IEF and directed that it be funded by contributions from the retirement system's defined benefit plans, the movement of funds from the IEF was accomplished by amending that same ordinance.

The Michigan Constitution provides that a county may adopt a charter that provides the county with powers conferred upon it by law: "Any county may . . . adopt . . . a county charter in a manner and with powers and limitations to be provided by general law." Const 1963, art 7, § 2. The Michigan Constitution also confers upon charter county legislatures the power to pass local laws related to local concerns: "Subject to law, a county charter may authorize the county through its regularly constituted authority to adopt resolutions and ordinances relating to its concerns." *Id.*

The Charter Counties Act ("CCA") includes a number of requirements for charter counties, including provisions that are required to be part of every county charter. See, e.g., MCL 45.514.[16] One of the CCA's requirements is that a county charter must provide for a retirement system (if the county already had one prior to the time the charter was adopted, which is the case for Wayne County) and may not preclude future modification of the retirement system:

> [A county charter must provide for] [t]he continuation and implementation of a system of pensions and retirement for county officers and employees in those counties having a system in effect at the time of the adoption of the charter. The system provided under the charter shall recognize the accrued rights and benefits of the officers and employees under the system then in effect. The charter shall not infringe upon nor be in derogation of those accrued rights and benefits. The charter shall not preclude future modification of the system. [MCL 45.514(1)(e).]

Pursuant to the CCA, Wayne County adopted its charter effective January 1, 1983. See *Lucas v Wayne Co Election Comm*, 146 Mich App 742, 744; 381 NW2d 806 (1985). Article VI, § 6.111, of the Wayne County Charter addresses retirement. Pursuant to the requirements of MCL 45.514(1)(e), § 6.111 continues Wayne County's previously existing retirement system and also explicitly provides that the Wayne County Board of Commissioners may amend the County's retirement ordinance:

> The Wayne County Employees Retirement System created by ordinance is continued for the purpose of providing retirement income to eligible employees and survivor benefits. The County Commission may amend the ordinance, but an amendment shall not impair the accrued rights or benefits of any employee, retired employee, or survivor beneficiary.[17][Wayne County Charter § 6.111, App 327a.]

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[16] Consistent with the Michigan Constitution and the CCA, Wayne County Charter § 1.112 states in part that the County is "a body corporate [and] possesses home rule power enabling it to provide for any matter of County concern and all powers conferred by constitution or law upon charter counties or upon general law counties, their officers, or agencies." App 325-326a.

[17] The Court of Appeals identified many of these constitutional, statutory, and local sources of Wayne County's power and authority to enact the 2010 ordinance, and did not question that

Footnote continued on next page ...

Chapter 141 of the Wayne County Code of Ordinances (WCCO) governs retirement. WCCO § 141-1 provides, in relevant part, that "[t]he county employees' retirement system established effective December 1, 1944, is hereby continued and restated under authority of the Home Rule Charter for the county." App 328a. In its current form, the WCCO provides the requirements for multiple defined benefit plans, a defined contribution plan, a hybrid plan and the IEF. See WCCO §§ 141-10, 141-20 to 141-22.1, and 141-32, App 329-338a.

The 2010 ordinance amended the retirement ordinance that governs the IEF – WCCO § 141-32. Among other things, § 141-32 caused IEF assets to be debited from the IEF, credited back to the defined benefit plans, and counted as a partial offset to Wayne County's 2010-2011 ARC. The 2010 ordinance was not the first time Wayne County amended WCCO § 141-32. It also did so in 2000, when it deleted a requirement that if 13th checks were issued in a given year they must account for at least 20%, and no more than 50%, of the IEF.[18] Perhaps more significant is the retirement ordinance amendment that initially established the IEF, Enrolled Ordinance 86-284. Adopted on July 24, 1986, Enrolled Ordinance 86-284 transferred assets *from the defined benefit plans to the IEF* to create the initial pool of funds available in the IEF. (See Enrolled Ordinance 86-284, App 95-96a). The Wayne County Board of Commissioners adopted all of these amendments pursuant to the Wayne County Charter and the CCA.

The CCA also authorizes Wayne County to modify the provisions of county systems created and continued by Wayne County's charter and ordinances. In *Roberts v Wayne County*,

Footnote continued from previous page ...

Wayne County was fully authorized to amend its retirement ordinance. The Court of Appeals instead found that the 2010 ordinance's transfer of IEF funds to the defined benefits plans as a partial offset to the County's ARC violated PERSIA (and possibly Const 1963, art 9, § 24).

[18] As noted previously, the Retirement Commission participated in the drafting of the 2000 amendment and later, in 2003, the Retirement Commission rejected claims by retirees challenging the 2000 amendment that 13th checks were accrued financial benefits.

176 Mich App 192; 439 NW2d 331 (1989), the plaintiffs asserted that the CCA prohibited a county from modifying its civil service system and that only the Michigan Legislature had such authority. *Id.* at 194. Noting that under MCL 45.514(1)(f) "[t]he [county] charter shall not preclude future modification of the system," *Roberts* held that Wayne County could modify its civil service system:

> It would seem illogical for the statute to prohibit the charter from precluding future modification of the civil service system, as the above statute clearly does, and yet hold that future modification is also prohibited. . . . Clearly, one purpose of the charter counties act, MCL 45.501 *et seq.*; MSA 5.302(1) *et seq.*, was to give charter counties some degree of autonomy over county affairs. . . . [The] modifications [did not] violate MCL 45.514(1)(f). [*Id.* at 195-196.]

In *exactly* the same way, the CCA (along with the Michigan Constitution and the Wayne County Charter) authorizes Wayne County to modify its Retirement System, which includes the very IEF that the County created in the first place.

### C. The 2010 ordinance does not violate Article 9, § 24 of the Michigan Constitution, the CCA, or the Wayne County Charter because it does not impair the "accrued financial benefits" of Retirement System participants or beneficiaries.

Of course, no amendment to Wayne County's retirement ordinances can impair the "accrued financial benefits" of Retirement System participants or their beneficiaries. See Const 1963, art, 9 § 24. See also MCL 45.514(1)(e) ("The charter shall not infringe upon nor be in derogation of those accrued rights and benefits."); Wayne County Charter § 6.111, App 327a ("[A]n amendment shall not impair the accrued rights or benefits of any employee, retired employee, or survivor beneficiary."). The 2010 ordinance, however, does not violate any of those restrictions for the simple reason that 13th checks are not "accrued financial benefits," a conclusion that is compelled by *Studier v Mich Pub Sch Employees' Retirement Bd*, 472 Mich 642; 698 NW2d 350 (2005), and *In re Request for Advisory Opinion Regarding Constitutionality* *of 2011 PA 38*, 490 Mich 295; 806 NW2d 683 (2011), which addressed art 9, §24, and whose analyses apply equally to MCL 45.514(1)(e) and Wayne County Charter § 6.111.[19]

**1. An "accrued" benefit is one that increases or grows over time and that arises on account of past service, yet the discretionary decision whether to issue a 13th check in a given year is not made until after retirement, and the amounts can vary from year to year.**

The Michigan Constitution provides:

> The accrued financial benefits of each pension plan and retirement system of the state and its political subdivisions shall be a contractual obligation thereof which shall not be diminished or impaired thereby.
>
> Financial benefits arising on account of service rendered in each fiscal year shall be funded during that year and such funding shall not be used for financing unfunded accrued liabilities. [Const 1963, art 9, § 24.]

As this Court has explained, "[t]hese two clauses unambiguously prohibit the state and its political subdivisions from diminishing or impairing 'accrued financial benefits,' and require them to fund 'accrued financial benefits' during the fiscal year for which corresponding services are rendered." *Studier*, 472 Mich at 649-650.

*Studier* examined the term "accrued financial benefit" in art 9, § 24. Focusing its attention on the term "accrued,"[20] this Court explained that art 9, § 24 "only protects those

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[19] Although Plaintiffs did not allege a violation of the "accrued rights" or "accrued benefits" provisions of MCL 45.514(1)(e) and Wayne County Charter § 6.111, Wayne County addresses those provisions because (1) they are found within the CCA and Wayne County Charter provisions authorizing the 2010 ordinance, and (2) provide the same protection as art 9, § 24.

[20] Because it is interpreting a constitutional provision, *Studier* interprets the word "accrued" as it would have been understood by the ratifiers of the Michigan Constitution. Yet the term "accrued" has the same meaning today as it did when the constitution was ratified, so *Studier*'s interpretation of the terms "accrued" and "accrued benefits" is controlling regardless of whether they are being interpreted as used in art 9, § 24, the CCA, or the Wayne County Charter. See *Merriam-Webster Online Dictionary* <http://www.merriam-webster.com/dictionary/accrued> (accessed May 8, 2014) (defining "accrue" as "to increase in value or amount gradually as time passes: to grow or build up slowly").

financial benefits that increase or grow over time." *Id.* at 654. The Court concluded that health care benefits paid to public school retirees did not constitute "accrued financial benefits" because the health care benefits did not "increase or grow over time" and thus were not "accrued" benefits:

> The ratifiers of our Constitution would have commonly understood "accrued" benefits to be benefits of the type that increase or grow over time—such as a pension payment or retirement allowance that increases in amount along with the number of years of service a public school employee has completed. Health care benefits, however, are not benefits of this sort. Simply stated, they are not accrued. . . . [N]either the amount of health care benefits a public school employee receives nor the amount of the premium, subscription, or membership fee that MPSERS pays increases in relation to the number of years of service the retiree has performed. [*Id.* at 654.]

*Studier* also held that such benefits "do not qualify as 'financial' benefits." *Id.* at 655. Although that aspect of *Studier* is not directly relevant here because 13th check payments certainly do qualify as "financial" benefits, what *is* helpful is the Court's reference to the comments of delegate Van Dusen during the constitutional convention, who stated that the intent of art 9, § 24 was to protect "the deferred compensation embodied in any pension plan." *Id.* at 657 (citations and internal quotation marks omitted). *Studier* found this statement to "reinforce[] our conclusion that the ratifiers would have commonly understood the phrase 'accrued financial benefits' to be one of limitation that would restrict the scope of protection provided by art 9, § 24 to *monetary payments for past services.*" *Id.* at 657-658 (emphasis added). As discussed further below, 13th checks have nothing to do with compensation for "past services." Rather, they are merely bonus checks that may be paid in a given year.

This Court again considered what is an "accrued financial benefit" in *In re Advisory Opinion,* 490 Mich 295, which involved a statute that eliminated a longstanding tax exemption for public pensions. Finding no violation of art 9, § 24, this Court observed that the "obvious intent of § 24" was to "ensure that public pensions be treated as contractual obligations that, once earned, could not be diminished" because "[b]efore § 24 was adopted, '[i]t had long been the general rule that pensions granted by public authorities were not contractual obligations but gratuitous allowances which could be revoked at will by the authority because the pensioner was not deemed to have had any vested right in their continuation.'" *Id.* at 311.

However, the Court explained, "Const 1963, art 9, § 24 . . . says nothing about whether these pension benefits can be taxed." *Id.* at 312. The Court thus examined whether a tax exemption could be considered an "'accrued financial benefit' of a pension plan." *Id.* at 313. The Court found that it could not, because a pension-tax exemption "does not 'grow over time'":

> During a state employee's working years, his or her pension-tax exemption, as opposed to the pension itself, cannot be said to be growing or accumulating because it does not even "come into existence" or "vest" until after the employee has retired and begins to collect his or her pension benefits. That is, one does not have a right to a tax exemption until one has received the funds that are subject to the exemption. Absent those funds, there is no tax exemption. And once a retiree has begun to receive his or her pension benefits, the tax exemption itself still does not "grow over time," but remains fixed. Therefore, a tax exemption is not an "accrued financial benefit." [*Id.* at 314-315.]

Like the pension-tax exemption in *In re Advisory Opinion*, the 13th checks that are funded from IEF assets do not "increase or grow over time." Thus, what this Court said about pension-tax exemptions in *In re Advisory Opinion* applies equally here. During a county employee's "working years," 13th check payments "cannot be said to be growing or accumulating because [they do] not even 'come into existence' . . . until after the employee has retired." *Id.* at 314. For that reason, 13th checks also do not represent deferred compensation for past services. See *Studier*, 472 Mich at 657-658. Nor do 13th checks "grow over time" in retirement. In fact, as even the Court of Appeals acknowledged, 13th check payments fluctuate from year to year, at times even decreasing. See *Wayne County*, 301 Mich App at 18-19.[21]

*Studier* further explained that accrued financial benefits "consist only of those '[f]inancial benefits arising on account of service rendered in each fiscal year.'" *Studier*, 472 Mich 655, quoting Const 1963, art 9, § 24. Specifically:

> [T]he first clause [of art 9, §24] contractually binds the state and its political subdivisions to pay for retired public employees' "accrued financial benefits . . . ." Thereafter, the second clause seeks to ensure that the state and its political subdivisions will be able to fulfill this contractual obligation by requiring them to set aside funding each year for those "financial benefits arising on account of service rendered in each fiscal year . . . ." Thus, because the second clause only requires the state and its political subdivision to set aside funding for "financial benefits arising on account of service rendered in each fiscal year" to fulfill their contractual obligation of paying for "accrued financial benefits," it reasonably follows that "accrued" financial benefits consist only of those "financial benefits arising on account of service rendered in each fiscal year . . . ." [*Studier*, 472 Mich at 654-655.]

Applying this concept, this Court in *In re Request for Advisory Opinion* concluded that a pension-tax exemption was not a benefit that arose "on account of service rendered in each fiscal year":

> [A] tax exemption is not an "accrued financial benefit" protected by § 24 because it would be impossible to fund a tax exemption, as opposed once again to the pension itself, in the year that the service was rendered in light of the fact that an exemption's value is entirely a function of the tax rate of the taxpayer at the time that the exemption is actually taken—something that obviously cannot be known at the time the services themselves are rendered. [*Id.* at 315.]

Like the pension tax exemption in *In re Advisory Opinion*, 13th checks do not arise "on account of service rendered in each fiscal year." *In re Advisory Opinion* explained that an accrued financial benefit cannot be one that arises "on account of service rendered in each fiscal year" unless it can be "fund[ed] . . . in the year that the service was rendered." *In re Advisory*

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[21] As discussed previously, Wayne County's retirement ordinance has, since its inception, always made the decision whether to even issue 13th checks entirely discretionary.

*Opinion*, 490 Mich at 315. Pension-tax exemptions did not meet that requirement because they are a function of "the tax rate of the taxpayer at the time that the exemption is actually taken," as opposed to when the employee's services are rendered. *Id.* Thus, it is "impossible to fund a tax exemption, as opposed . . . to the pension itself, in the year that the service was rendered." *Id.* The same analysis applies to 13th checks. They cannot be funded in the year service was rendered because the discretionary decision whether to make a 13th check distribution in a given year is not made until *after the employee retires*, in contrast to the employee's regular pension, which is calculated and funded during his or her working years.

Under *In re Advisory Opinion*, any "benefit" that is determined *after* an employee retires cannot be one that arises "on account of service rendered in each fiscal year." *Hannan v Detroit City Council*, unpublished opinion per curiam of the Court of Appeals, issued September 1, 2000; 2000 Mich App LEXIS 980 (Docket No. 211704) (App 319-323a), addressed whether Const 1963 art 9, § 24, was violated when the Detroit City Council passed ordinances increasing the benefits of certain "qualified retirees." *Id.* at *1, App 319a. *Hannan* held that art 9, § 24 *did not even apply* to ordinances because they only affected "retirees and not those that are currently working and accruing financial benefits," i.e., they conferred a benefit "that was not earned during the year the benefit was given." *Id.* at *7, App 321a.

Similarly, the decision whether to distribute 13th checks in a given year, including the amounts of those distributions, is made only *after* an employee retires. As a result, they "confer a benefit that was not earned during the year the benefit was given," and art 9, § 24, simply does not apply to them.

### 2. The Court of Appeals' dicta suggesting that there might be a "group" accrued financial benefit is a dangerous precedent that this Court cannot let stand.

Although the Court of Appeals did not find the 2010 ordinance violated either Const 1963, art 9, § 24, the CCA, or Wayne County's charter, it suggested in dicta that "from a broad perspective, taking into consideration not individual retirees or survivor beneficiaries but all of them together as a group, the 13th-check program itself could arguably be viewed as an accrued financial benefit for purposes of the first clause contained in Const 1963, art 9, § 24, which benefit was diminished and impaired by the transfer of $32 million out of the IEF." *Wayne County*, 301 Mich App at 35 n 23; see also *id.* at 40. The Court of Appeals made those statements even though it held, correctly, that "payment of a 13th check cannot be viewed as an accrued financial benefit, where there is no vested or enforceable right to a 13th check given the discretionary distribution language that has always been part of the IEF ordinance, along with the lack of any CBA language requiring disbursement of a 13th check." *Wayne County*, 301 Mich App at 34.

The Court of Appeals could not logically conclude on one hand that an individual 13th check is not an "accrued financial benefit," but then suggest, on the other, that the "13th check program" can somehow be considered a "group" entitlement. Neither *Studier* nor *In re Advisory Opinion* distinguished between an "individual" and a "group" accrued financial benefit, and the Court of Appeals cited no other authority for its novel proposition. Nor is there support for it in art 9, § 24 or the constitutional convention debates, which confirm that the people ratifying art 9, § 24 would have understood an "accrued financial benefit" to be an *individual right belonging to the employee*. As delegate Van Dusen observed:

> MR. VAN DUSEN: . . . I would like to indicate that the words 'accrued financial benefits' were used designedly, so that *the contractual right of the employee* would be limited to the deferred compensation embodied in any pension

> plan, and that we hope to avoid thereby proliferation of litigation by individual participants in retirement systems talking about the *general benefits structure*, or something other than his *specific right to receive benefits*. It is not intended that an individual employee should, as a result of this language, be given the right to sue the employing unit to require the actuarial funding of past service benefits, or anything of that nature. What it is designed to do is to say that *when his benefits come due, he's got a contractual right to receive them.*
>
> . . . [H]e has the contractual right to sue for them. *So that he has no particular interest in the funding of somebody else's benefits so long as he has the contractual right to sue for his.* [1 Official Record, Constitutional Convention 1961, pp 773-774 (emphasis added).][22]

In any event, it is irrelevant whether 13th checks are viewed from the perspective of an individual employee or that of a "group." Either way, *Studier* and *In re Advisory Opinion* are controlling, and establish that there can be no "accrued financial benefit" unless the benefit in question increases or grows over time and can be funded "in the year that service was rendered." The "13th check program" simply does not meet those requirements.

In sum, the Michigan Constitution, CCA, and Wayne County Charter authorized Wayne County to create and to modify the Retirement System, including the transfer of IEF funds back into the defined benefit plans, and the County did not impair any "accrued" financial benefits in doing so.

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[22] In *Studier*, this Court found it appropriate to rely on the statements of delegate Van Dusen "to shed light on why [the delegates] chose to employ the particular terms they used in drafting the provision to aid in discerning what the common understanding of those terms would have been when the provision was ratified by the people." *Studier*, 472 Mich at 656-657. See also *id.* at 657 (finding delegate Van Dusen's statements to be "directly relevant to discerning the common understanding of the words 'accrued' and 'financial' at the time of the constitutional convention").

**D. RESPONSE TO ISSUE #2: The 2010 ordinance, which moved IEF assets back to the defined benefit plans, does not violate PERSIA – with or without a corresponding offset to the County's ARC – because (1) the assets in that *intra-system* transfer were all used for the exclusive benefit of retirement system participants and beneficiaries, and (2) such a transfer is not a "transaction" (prohibited or otherwise).**

The Court of Appeals relied on two specific provisions of PERSIA when it invalidated the 2010 ordinance's transfer of IEF assets to the defined benefit plans as a partial offset to the County's 2010-2011 ARC. *First,* the Court of Appeals concluded that the transfer and offset violates PERSIA's "exclusive benefit" rule, MCL 38.1133(6) (now MCL 38.1133(8)). *Second,* the Court concluded that the transfer and offset violates PERSIA's "prohibited transaction" rule, MCL 38.1133(6)(c) (now MCL 38.1133(8)(c)). The Court of Appeals also stated that even without the offset – in other words, even if IEF assets are merely transferred back into the defined benefit plans – the 2010 ordinance would still violate PERSIA because Wayne County would still receive a benefit, ostensibly because allocating additional funds to the defined benefit plans would result in a recalculated and reduced ARC.[23] Each of the Court of Appeals' conclusions are wrong.

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[23] The Court Appeals explained:

> We note that count II of the County's counterclaim asserted in part that even if the offset is determined to violate PERSIA, the debiting of the $32 million from the IEF and crediting of that amount to the defined benefit plan assets could survive invalidation of the offset. In other words, $32 million should still be added to the defined benefit plan assets and removed from the IEF, but the County would simply not be able to receive the $32 million ARC offset and savings. To the extent that this opinion has not already disposed of this argument, we reject it, as the County would still receive a benefit by additional funds being allocated to the defined benefit plan assets. Indeed, in the context of the County's cross-appeal and its argument that it has standing to raise fiduciary-duty claims, the County contends that it incurred a special injury and had a substantial interest that was detrimentally affected because of the effect on the ARC when the Retirement Commission failed to allow more funds to remain with the defined benefit plan

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### 1. The 2010 ordinance does not violate PERSIA's "exclusive benefit" rule.

#### a) Retirement system assets never left the Retirement System and always remained for the exclusive benefit of participants and their beneficiaries.

PERSIA's exclusive benefit rule provides that "*[t]he system* shall be a separate and distinct trust fund and the assets *of the system* shall be for the exclusive benefit of the participants and their beneficiaries and of defraying reasonable expenses of investing the assets of the system." MCL 38.1133(6) (emphasis added). The Court of Appeals held that the 2010 ordinance violated the exclusive benefit rule when it made an intra-system transfer of funds from the IEF back into the defined benefit plans because Wayne County received "an enormous cost savings benefit" in the form of a partial offset to the county's annual required contribution ("ARC"), which "freed up County funds for other uses." *Wayne County*, 301 Mich App at 32. In the Court of Appeals' view, this meant that the Retirement System's assets were not being used for the "exclusive" benefit of the participants and their beneficiaries. *Id.* at 31-33.

The Court of Appeals misconstrued the plain meaning of MCL 38.1133(6) by taking the term "exclusive benefit" out of context.[24] "Exclusive benefit" refers to the Retirement System's "assets" and says they "shall be for the exclusive benefit of the participants and their

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> assets, instead funneling the money to the IEF under its discretionary authority [*Wayne County*, 301 Mich App at 51 n 29.]

[24] This Court has explained that a "statutory term cannot be viewed in isolation, but must be construed in accordance with the surrounding text and the statutory scheme." *Breighner v Mich High School Athletic Ass'n*, 471 Mich 217, 232; 683 NW2d 639 (2004). A statutory term like "exclusive benefit" "does not stand alone, and thus it cannot be read in a vacuum." *Sweatt v Dep't of Corrections*, 468 Mich 172, 179; 661 NW2d 201 (2003). "[I]t exists and must be read in context with the entire act, and the words and phrases used there must be assigned such meanings as are in harmony with the whole of the statute, construed in the light of history and common sense." *Id.* (citation omitted).

beneficiaries." MCL 38.1133(6) is not concerned with whether the employer's own interests are also advanced in some way, so long as the Retirement System's "assets" (i.e., its "cash and investments") are for the "exclusive benefit" of the participants and their beneficiaries. Under the plain language of MCL 38.1133(6), the "exclusive benefit" rule can only be violated if a system's "assets" are "shared with others" (which is how the Court of Appeals defined "exclusive," see *Wayne County*, 301 Mich App at 31). Here, that indisputably did not happen. As the Court of Appeals conceded, the "assets" at issue, "once part of the IEF and now part of the defined benefit plan assets on the accounting records, *were still to be used for the benefit of participants and their beneficiaries in the form of regular pension payments.*" *Wayne County*, 301 Mich App at 32 (emphasis added).

There is no question that one of the "effects" of transferring IEF assets back to the defined benefit plans is to reduce Wayne County's own contribution to the defined benefit plans. The 2010 ordinance does that directly by offsetting Wayne County's ARC on a dollar-for-dollar basis. But even without such an express offset, transferring IEF assets to the defined benefit plans would still reduce Wayne County's ARC: with $32 million added to the defined benefit plans, the ARC would need to be re-calculated and unquestionably would be reduced. Either way, the reduction of Wayne County's ARC – whether through a direct offset or a recalculation of the ARC – is not the sort of "benefit" that MCL 38.1133(6) addresses in providing that "assets" of a retirement system shall be for the "exclusive benefit" of participants and their beneficiaries. While transferring assets inevitably has an impact that is "beneficial to the County" (the phrase used by the Court of Appeals), 100% of the Retirement System assets remained for the exclusive benefit of participants and beneficiaries. The Retirement System's "assets" were never used for any purpose other than to pay benefits to Retirement System participants and their beneficiaries, which is all that MCL 38.1133(6) is concerned with.

The Court of Appeals asserted that the "Retirement System unquestionably lost $32 million." *Wayne County*, 301 Mich App at 33. But that mischaracterizes the effect of the ordinance. No "assets" were removed from the Retirement System, and all of the assets remained for the exclusive benefit of participants and beneficiaries. Wayne County simply transferred funds from the discretionary IEF to the defined benefit plans as a partial offset of its ARC for the 2010-2011 fiscal year. It is true that without the 2010 ordinance, the Retirement System's "assets" would have been *increased* by an additional $32 million, but whether funds should have been added to the system has nothing to do with whether its *existing* "assets" remained for the exclusive benefit of participants and beneficiaries, which is all the statute is concerned with.[25] Although transferring IEF assets back to the defined benefit plans reduced Wayne County's ARC, with or without a corresponding offset, such a one-time *savings* to the County did not affect whether the Retirement System assets remained for the exclusive benefit of participants and beneficiaries. On the contrary, the "assets" in the Retirement System have always been used – as even the Court of Appeals acknowledged – only to pay benefits to retirement system participants and their beneficiaries, exactly as MCL 38.1133(6) required.

Instead of carefully analyzing MCL 38.1133(6), what really drove the Court of Appeals' exclusive benefit analysis was protection of *the IEF*, not the assets of the Retirement System. The Court of Appeals characterized the IEF as a "reserve" that was "dedicated" to "13th check distributions" as though it were somehow distinct from the Retirement System:

[25] It is also important to note that because the 2010 ordinance resulted in the payment of the County's 2010-2011 ARC, the defined benefit plans were no less funded than they would have been without the 2010 ordinance. All that changed is that the discretionary IEF bonus fund was reduced.

> [O]nce a particular dollar amount, if any, was arrived at under the IEF formula, including the discretionary components controlled by the Retirement Commission, the IEF ordinance had always *compelled or mandated* the allocation or crediting of said amount to the IEF. And the assets in the IEF were dedicated for use by retirees and survivor beneficiaries in the form of a 13th check as a hedge against inflation. By September 30, 2010, the IEF had an accumulated balance of approximately $44 million that was intended and designated for 13th-check distributions; indeed, there had never been, for the most part, any other permitted use of IEF assets. The IEF, in and of itself, can be accurately characterized as a reserve belonging to and vested in the Retirement System's participants as a whole, outside the reach of defendants, to be used to assist retirees and survivor beneficiaries in fighting the devaluing of the dollar by inflation. [*Wayne County*, 301 Mich App at 34-35.]

The Court of Appeals noted that as a result of the 2010 ordinance, the IEF's balance was "decreased by $32 million down to $12 million," and asserted that the 2010 ordinance "improperly invaded the *assets of the IEF*" and "depleted and redirected *IEF assets* that had been designated for . . . payment of 13th checks." *Wayne County*, 301 Mich App at 34-38 (emphasis added).

Treating "the IEF" as inviolate ignores that it is merely a fund *within the Wayne County Retirement System.* Nothing in MCL 38.1133(6)'s "exclusive benefit" rule prevents an employer from *reallocating the assets inside a retirement system*, as long as those assets within the Retirement System remain for the exclusive benefit of participants and beneficiaries. Again, MCL 38.1133(6) requires nothing more than that "*assets of the system* shall be for the exclusive benefit of the participants and their beneficiaries." (Emphasis added). Nothing in the plain language of the statute requires that assets in the IEF remain dedicated to purposes *specific to the IEF*, i.e., to pay discretionary bonuses. Thus, the fact that the $32 million transferred from the IEF back into the defined benefit plans was not used *to distribute 13th checks* does not mean that the "system's assets" were somehow treated as being other than for the exclusive benefit of Retirement System participants and their beneficiaries. The Court of Appeals erred in concluding otherwise.

### b) The Court of Appeals' "exclusive benefit" analysis disregards MCL 38.1140m, which expressly permits transfers and offsets similar to that under the 2010 ordinance.

The Court of Appeals' interpretation of MCL 38.1133(6) is also incompatible with MCL 38.1140m, which expressly permits transfers and offsets similar to that of the 2010 ordinance. MCL 38.1140m provides that "[i]n a plan year, any current service cost payment may be offset by a credit for amortization of accrued assets, if any, in excess of actuarial accrued liability." Thus, as the Court of Appeals was forced to concede, MCL 38.1140m specifically *authorizes* the very sort of offset that the Court found MCL 38.1133(6) to *prohibit*. In fact, the Court of Appeals expressly recognized that an offset under MCL 38.1140m "could be viewed as being used for the benefit of the public employer by effectively diminishing the employer's ARC." *Wayne County*, 301 Mich App at 37. The only difference between MCL 38.1140m and the 2010 ordinance is that MCL 38.1140m applies only to offsets using "accrued assets" held within a traditional defined benefit plan during a period of overfunding, whereas the offset under the 2010 ordinance applies only to assets held in the discretionary IEF.[26]

Instead of construing MCL 38.1133(6) in harmony with MCL 38.1140m, the Court of Appeals tersely and summarily dismissed MCL 38.1140m as an *exception* to MCL 38.1133(6) that is "not implicated with respect to the offset in the 2010 ordinance." *Id.* The Court of Appeals erred because it creates an unnecessary conflict between MCL 38.1133(6) and MCL 38.1140m.

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[26] Because IEF assets are not included in the Retirement Commission's calculation of the defined benefit plans' accrued assets or actuarially accrued liabilities, and are instead used solely for the purpose of making discretionary 13th check distributions, MCL 38.1140m is not implicated here, as the trial court correctly determined and as the Court of Appeals conceded. See *Wayne County*, 301 Mich App at 54 ("MCL 38.1140m appears to only address ARCs relative to defined benefit plans . . . .").

Although it is well-recognized that "'where a statute contains a general provision and a specific provision, the specific provision controls,'" *Duffy v Dep't of Natural Resources*, 490 Mich 198, 215; 805 NW2d 399 (2011) (citation omitted), that canon applies only when statutory provisions "seemingly conflict." See *Frame v Nehls*, 452 Mich 171, 176 n 3; 550 NW2d 739 (1996). There is no "conflict" between MCL 38.1133(6) and MCL 38.1140m under Wayne County's and the trial court's construction. The Court of Appeals *should have* applied the established statutory interpretation principle that courts must read provisions of a statute together "to produce an harmonious whole and to reconcile any inconsistencies wherever possible." *World Book v Mich Dep't of Treasury*, 459 Mich 403, 416; 590 NW2d 293 (1999). Instead of viewing the offset permitted under MCL 38.1140m as an exception to the exclusive benefit rule, the Court of Appeals should have viewed it as being consistent with the notion that so long as Retirement System assets remain for the exclusive benefit of participants and beneficiaries through paying benefits, there is no violation of the "exclusive benefit" rule.

**c) The Court of Appeals' "exclusive benefit" analysis contradicts persuasive authority from outside of Michigan, including the United States Supreme Court's interpretation of ERISA's similar "exclusive benefit" rule.**

ERISA's "exclusive benefit" rule is substantially similar to PERSIA's, providing that "the assets of a plan shall never inure to the benefit of any employer and shall be held for the exclusive purposes of providing benefits to participants in the plan and their beneficiaries and defraying reasonable expenses of administering the plan." 29 USC 1103(c)(1). The United States Supreme Court has held that as long as retirement system assets are ultimately used for the exclusive purpose of paying benefits, there is no violation of ERISA's "exclusive benefit" rule.

The Supreme Court's precedents construing ERISA are highly persuasive because of the similarities between ERISA's exclusive benefit rule and MCL 38.1133(6).[27]

In *Hughes Aircraft Co v Jacobson*, 525 US 432; 119 S Ct 755; 142 L Ed 2d 881 (1999), the plaintiffs claimed that Hughes violated ERISA's exclusive benefit rule (a/k/a "anti-inurement" provision) by amending a company pension plan, which had a surplus of assets, to establish an early retirement program that "provided significant additional retirement benefits to certain eligible active employees," as well as a new noncontributory benefit structure whereby "new participants could not contribute to the [p]lan, and would thereby receive fewer benefits. Existing members could continue to contribute or opt to be treated as new participants." *Id.* at 436. The plaintiffs claimed that these changes resulted in Hughes' use of the plan's surplus assets to cover its own funding obligations, and that Hughes thus violated ERISA's exclusive benefit rule by "benefiting itself at the expense of the Plan's surplus." *Id.* at 437, 441-442.

The Supreme Court, in a *unanimous opinion*, held that because Hughes continued to use plan assets for the sole purpose of paying its obligations to the plan's beneficiaries, Hughes "could not have violated" the exclusive benefit rule because "the [exclusive benefit rule] focuses exclusively on whether fund assets were used to pay pension benefits to plan participants." *Id.* at 442-443. *Hughes* held that using plan assets to pay obligations to plan beneficiaries is, by definition, a use of plan assets for the exclusive benefit of participants:

> Respondents do not dispute that Hughes used fund assets for the sole purpose of paying pension benefits to plan participants. . . . Because . . . respondents do not

[27] See, e.g., *Quinn v Police Officers Labor Council*, 456 Mich 478, 482 n 1; 572 NW2d 641 (1998) ("Because our state labor statutes are patterned after the National Labor Relations Act, we examine federal construction of analogous provisions of the NLRA for guidance in construing our own labor statutes."); *Evening News Ass'n v City of Troy*, 417 Mich 481, 495; 339 NW2d 421 (1983) ("[T]he similarity between the [Michigan Freedom of Information Act] and the federal act invites analogy when deciphering the various sections.") (citations and internal quotation marks omitted).

> allege that Hughes used any of the assets for a purpose other than to pay its obligations to the Plan's beneficiaries, Hughes could not have violated the anti-inurement provision under ERISA § 403(c)(1). [*Id.* at 442-443.]

Since *Hughes*, the Supreme Court has confirmed that 28 USC 1103(c)(1) "demands only that plan assets be held for supplying benefits to plan participants." *Raymond B Yates, MD, PC Profit Sharing Plan v Hendon*, 541 US 1, 22; 124 S Ct 1330; 158 L Ed 2d 40 (2004).

Given the striking similarity between 29 USC 1103(c)(1) and MCL 38.1133(6), and the factual parallels between *Hughes* and the present case, the Court of Appeals should have followed its reasoning in construing MCL 381133(6). The Court of Appeals instead casually dismissed *Hughes* and ineffectively tried to distinguish it.

The Court of Appeals first observed that the plaintiffs in *Hughes* were found to have "no entitlement to share in a plan's surplus – even if it is partially attributable to the growth of their contributions," whereas "[h]ere, retirees and survivor beneficiaries *as a group* had an entitlement to share in the IEF assets at some juncture, as those assets had been specifically allocated and were intended for distribution to retirees and survivor beneficiaries in the form of 13th checks." *Wayne County*, 301 Mich App at 40, citing *Hughes*, 525 US at 440. Wayne County already discussed in detail the plain error in the Court of Appeals' novel and unsupported "group" entitlement theory. Moreover, whether or not the plaintiffs in *Hughes* were entitled to share in surplus plan assets had nothing whatsoever to do with the Supreme Court's analysis of 29 USC 1103(c)(1).

The Court of Appeals also said *Hughes* involved use of "surplus assets" that were "never earmarked for anything but the future distribution of defined benefit plan payments to retirees in general," whereas "the $32 million in the IEF that was shifted to the defined benefit plan assets simply did not constitute true 'surplus' assets." *Wayne County*, 301 Mich App at 41. Instead, the Court of Appeals reasoned, the defined benefit plans were "severely underfunded," and while the assets in the defined benefit plans and IEF were "pooled together in a single trust fund," the IEF's assets were "segregated in terms of accounting records" and "primarily intended and designed for the payment of 13th checks." *Id.* *First*, that superficial "distinction," disregards *Hughes'* holding that the exclusive benefit rule is not violated if plan assets, "surplus" or not, go to the exclusive purpose of paying benefits to the participants.[28]

*Second*, the Court of Appeals treats the IEF as though it were its own independent retirement "system," when the IEF is merely one "fund" *within* the Retirement System from which assets were transferred to another part of the system. Federal courts have long held that such intra-system transfers do not violate the exclusive benefit rule, and nothing in MCL 38.1133(6) compels a different result. See *United Mine Workers of Am Health & Ret Funds v Robinson*, 455 US 562, 572; 102 S Ct 1226; 71 L Ed 2d 419 (1982) (construing requirement under § 302(c)(5) of Labor Management Relations Act that employee benefit trust fund be used for the "sole and exclusive benefit of the employees . . . and their families and dependents," holding that it does not preclude "allocation of the funds among the persons protected"); *Holliday v Xerox Corp*, 732 F2d 548, 549-552 (CA 6, 1984) (holding ERISA's exclusive benefit rule not violated by "the transfer of funds from one pension account to another *within the company's pension plan*, and the subsequent use of those funds as a setoff in calculating the retirement income owed to employees under [a] new guaranteed minimum retirement income plan") (emphasis added).

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[28] The Supreme Court did allude to the fact that "all times, Hughes satisfied its continuing obligation under the provisions of the Plan and ERISA to assure that the Plan was adequately funded," and that Hughes therefore "did not act impermissibly by using surplus assets from the contributory structure to add the noncontributory structure to the Plan." *Hughes*, 525 US at 442. But the same can be said here, as Wayne County has always met its defined benefit plan funding obligations. As with the pension plan changes in *Hughes*, the 2010 ordinance did not impact the defined benefit plans' funded status.

The Court of Appeals further tried to distinguish *Hughes* from the 2010 ordinance because the ordinance provided a benefit to Wayne County that was more than "incidental," which it defined as "happening or likely to happen in an unplanned or subordinate conjunction with something else," or "incurred casually and in addition to the regular or main amount." *Wayne County*, 301 Mich App at 43-44, citing *Random House Webster's College Dictionary* (2001)) (internal quotation marks omitted). According to the Court of Appeals, "[i]t cannot honestly and reasonably be disputed that the main purpose of the 2010 ordinance was to benefit the County by reducing the amount of money that the County had to directly pay to satisfy the ARC," and that this "benefit" was "certainly not unplanned or incurred casually." *Id.* The Court of Appeals missed the mark completely. Although *Hughes* alluded that "incidental benefits" to an employer were permissible, *Hughes'* persuasive value does not depend on whether reducing Wayne County's ARC can be characterized as an "incidental benefit."[29] Under MCL 38.1133(6), and consistent with *Hughes*, the exclusive benefit rule is met so long as retirement system assets do not go "for a purpose other than to pay [the systems'] obligations to [its] beneficiaries." *Hughes* does not suggest that the exclusive benefit rule depends on evaluating either the employer's purported motivation for amending a retirement plan or the monetary value of any effect of the amendment. Under *Hughes*, the question is simply "Did plan assets go to some purpose other than paying benefits?" If not, there is no violation of the exclusive benefit rule. By going beyond that, the Court of Appeals plainly erred.

The Court of Appeals misunderstood *Hughes* as standing for the "unremarkable proposition that an employer, for purposes of ERISA, can use surplus defined benefit plan assets

[29] Indeed, the "incidental benefits" were never even quantified in *Hughes* because their monetary value was irrelevant. But needless to say, the employer's savings that were deemed "incidental" in *Hughes* would likely have been tens of millions of dollars.

as an offset against required contributions." *Id.* at 44. Nowhere did *Hughes* suggest that its exclusive benefit rule analysis turned on whether "surplus defined benefit plan assets" were being used "as an offset against required contributions." *Hughes* held there is no violation of the exclusive benefit rule so long as plan assets go to pay retirement benefits. The Court of Appeals missed *Hughes*' point entirely.

The Court of Appeals also misunderstood *Claypool v Wilson*, 4 Cal App 4th 646; 6 Cal Rptr 2d 77 (1992). In *Claypool*, the court rejected a claim that the California legislature violated California's exclusive benefit rule and otherwise "invaded" funds "held in trust for the benefit of [California Public Employees' Retirement System ("PERS")] members" when it repealed supplemental cost-of-living (COLA) programs and "direct[ed] that the funds be used to offset contributions otherwise due from PERS employers." *Id.* at 652, 660-661. *Claypool* held that this did not violate California's exclusive benefit rule, which provides that "[t]he assets of a public pension or retirement system are trust funds and shall be held for the exclusive purposes of providing benefits to participants in the pension or retirement system and their beneficiaries and defraying reasonable expenses of administering the system."[30] The court reasoned that using the former supplemental COLA funds to reduce the employer contributions otherwise necessary to keep the retirement system "in actuarial trim does not invade" the retirement system because the funds "continue to be 'held for the exclusive purposes of providing benefits to participants . . . .'" *Id.* at 674 (citation omitted).

In wrongly dismissing *Claypool* as an "aberration," the Court of Appeals ineffectively tried to distinguish it even though the 2010 ordinance's credit and offset is functionally the same as that upheld in *Claypool*. Like the California legislature's action in *Claypool*, the 2010

[30] See Cal Const, Art XVI, § 17. At the time of *Claypool*, this provision was worded a little differently, but is substantively the same.

ordinance did not authorize the use of Retirement System assets for *Wayne County's* benefit. On the contrary, the assets never left the Retirement System. They were merely transferred to the defined benefit plans for the direct benefit of the plans' participants, just as in *Claypool.*

In distinguishing *Claypool*, the Court of Appeals primarily relied on certain language used in the former COLA programs to alert participants to the possibility that their availability may be "limited." *Wayne County*, 301 Mich App at 46. But an examination of *Claypool* reveals that this "limiting or restrictive language" had nothing whatsoever to do with the *Claypool* court's exclusive benefit rule analysis.

The Court of Appeals also said that although the California legislature enacted a "new alternative COLA program," there were "no comparable new advantages to county retirees [under the 2010 ordinance]; the 13th check program was eviscerated absent mandatory reimbursement of the $32 million." *Id.* In drawing that distinction, the Court of Appeals cited a single passage from *Claypool* that "[t]he saving of public employer money is not an illicit purpose if changes in the pension program are accompanied by comparable new advantages to the employee." *Id.*, citing *Claypool*, 4 Cal App 4th at 665. But that comment from *Claypool* came from an entirely different part of the court's opinion addressing whether the California Legislature's modification of the supplemental COLA programs was "reasonable." It played no part in the *Claypool* court's discussion of the exclusive benefit rule.

Rather than straining to distinguish or otherwise avoid *Hughes* and *Claypool*, the Court of Appeals should have viewed those decisions as persuasive indicators that its proposed exclusive benefit rule analysis was unsound. Instead, the Court of Appeals adopted a distorted view of the exclusive benefit rule that no other court has embraced.

The plain language of MCL 38.1133(6), the substantially-similar offset explicitly provided under MCL 38.1140m, and *Hughes* and *Claypool* all lead to the undeniable conclusion that the "exclusive benefit" rule does not prohibit the advancement of the employer's own interests in some way so long as the system's actual "assets" (i.e., its "cash and investments") are not "shared with others." With or without the corresponding offset to Wayne County's ARC, transferring IEF funds back to the defined benefit plans did not cause retirement system assets to be shared with others because the assets never left the Retirement System. The Retirement System's assets, including those in the IEF, always remained for the exclusive benefit of paying participants and beneficiaries. There was no violation of the "exclusive benefit" rule.

### 2. RESPONSE TO ISSUE #3: Moving IEF funds to the defined benefit plans is an intra-system transfer, not a transaction between the Retirement System and another party, and thus is not a "transaction" within the meaning of MCL 38.1133(6).

The Court of Appeals also erred when it concluded that transferring IEF assets to the defined benefit plans was a "transaction" in violation of MCL 38.1133(6)(c), which prohibits a fiduciary from causing the system "to engage in a transaction if he or she knows that the transaction is . . . , either directly or indirectly[,] . . . [a] transfer to, or use by or for the benefit of, the political subdivision sponsoring the system of any assets of the system for less than adequate consideration."

#### a) A "prohibited transaction" is a transaction involving the Retirement System and *another party*, and not a purely intra-system transfer of assets.

Although the Court of Appeals focused on subsection (c), MCL 38.1133(6) prohibits several kinds of "transactions" between a retirement system and either a "party in interest" or the "political subdivision sponsoring the system":

> With respect to a system, an investment fiduciary shall not cause the system to engage *in a transaction if* he or she knows or should know that *the transaction is* any of the following, either directly or indirectly:
>
> (a) A sale or exchange or leasing of any property from the system to a party in interest for less than fair market value, or from a party in interest to the system for more than the fair market value.
>
> (b) A lending of money or other extension of credit from the system to a party in interest without the receipt of adequate security and a reasonable rate of interest, or from a party in interest to the system with the provision of excessive security or at an unreasonably high rate of interest.
>
> (c) A transfer to, or use by or for the benefit of, the political subdivision sponsoring the system of any assets of the system for less than adequate consideration.
>
> (d) The furnishing of goods, services, or facilities from the system to a party in interest for less than adequate consideration, or from a party in interest to the system for more than adequate consideration. [MCL 38.1133(6)(a)-(d).]

The Court of Appeals erroneously assumed that MCL 38.1133(6)(c) applies to transfers of assets *within a Retirement System*. On the contrary, a plain reading of MCL 38.1133(6) reveals that it only applies to "transactions" between a "system's investment fiduciary" and *another party*. Subsections (a), (b), and (d) explicitly refer to transactions between the system and a "party in interest." Subsection (c) refers to transactions either (1) between the system and the "political subdivision sponsoring the system" (i.e., a "transfer to" or "use by" the system sponsor), or (2) between the system and another party that benefits the system sponsor (i.e., a "use . . . for the benefit of" the system sponsor).

Reading these four subsections together shows that MCL 38.1133(6) does not apply to *intra-system* transfers. This is further confirmed by subsection (c)'s prohibition against transferring or using system assets "for less than adequate consideration." "Adequate consideration" means transactions between a "system" and another party, and not a wholly intra-system transfer of assets. There is no support in the statutory language for the Court of Appeals' erroneous assumption that transferring assets from the IEF to the defined benefit plans was a "transaction."

### b) The 2010 ordinance does not result in any of the three types of "transactions" described in MCL 38.1133(6)(c).

Transferring IEF assets back to the defined benefit plans (with or without the corresponding offset to Wayne County's ARC) also did not involve any of the three transactions listed under MCL 38.1133(6)(c). MCL 38.1133(6)(c) prohibits (1) a "transfer" of any assets from the Retirement System "to" the system sponsor, (2) the "use" of any Retirement System assets "by" the system sponsor, and (3) the "use" of any Retirement System assets "for the benefit of" the system sponsor. None of these "transactions" occurred here.

With regard to the first type of prohibited transaction (i.e., a "transfer" of any assets from a Retirement System "to" the system sponsor), the Court of Appeals held, that the 2010 ordinance involved, "*effectively*, an unlawful transfer of assets to the County for use to satisfy obligations relative to the ARC." *Wayne County*, 301 Mich App at 48 (emphasis in original and citation omitted). However, the IEF assets indisputably *never left the Retirement System*, and they certainly were not transferred to Wayne County. The 2010 ordinance provides for an entirely *intra-system* assets transfer – from the Retirement System's IEF to its defined benefit plans.

MCL 38.1133(6)(c) does not address "effective" asset transfers; it prohibits *transfers*. The term "effectively" means "in an indirect way." *Merriam-Webster Online Dictionary* <http://www.merriam-webster.com/dictionary/effectively> (accessed May 8, 2014). Although the statute prohibits certain transfers whether done "directly or indirectly," it still requires a "transfer," which is defined as "to convey from one person, place, or situation to another." *Merriam-Webster Online Dictionary* <http://www.merriam-webster.com/dictionary/transfer>

(accessed May 8, 2014).[31] Under no construction did the 2010 ordinance transfer Retirement System assets from the Retirement System to Wayne County.

As to the second type of prohibited transaction in MCL 38.1133(6)(c) (a "use" of any Retirement System assets "by" the system sponsor), the Court of Appeals concluded that "the 2010 ordinance effectively . . . permitted or authorized the County to use . . . assets in the IEF." *Wayne County*, 301 Mich App at 47. But the "assets" were simply transferred from the IEF to the Retirement System's own defined benefit plans, where they were used exclusively to pay benefits to participants. Because the assets never left the Retirement System, they cannot be said to have been put to the County's own "use" – whether "effectively" or otherwise.

The Court of Appeals said the 2010 ordinance also violated the third type of "transaction" prohibited by MCL 38.1133(6)(c) (i.e., the "use" of retirement system assets "for the benefit of" the system sponsor), because "[w]e have already found, relative to our analysis of the exclusive benefit rule, that the County benefited greatly from the use of the excess IEF assets." *Wayne County*, 301 Mich App at 48. As discussed, however, it cannot be said that the system's "assets" were "use[d] . . . for the "benefit" of Wayne County because those assets were "used" solely for the payment of benefits to Retirement System participants and their beneficiaries.

The Court of Appeals mistakenly relied on *Hughes* in its "prohibited transaction" analysis. *Hughes* briefly alluded to the concept of a "sham transaction," which it defined as a transaction that is "meant to disguise an otherwise unlawful transfer of assets to a party in interest." *Hughes*, 525 US at 445. The Court of Appeals declared that transferring assets from

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[31] An "indirect" transfer would be a transfer to a third party, followed by a transfer from the third party to the plan sponsor. The point of specifying that "indirect" transfers are prohibited along with "direct" transfers is simply to avoid the use of a third party as a go-between. Even an "indirect" transfer still requires "assets" to actually leave the retirement system.

the IEF to the defined benefit plans as an offset to the County's ARC *was* a "sham transaction" because, in its view, it involved "*effectively*, an unlawful transfer of assets to the County." *Wayne County*, 301 Mich App at 48 (emphasis in original). But moving funds from the IEF to the defined benefit plans (with or without a corresponding offset to Wayne County's ARC) cannot be a "sham transaction" as *Hughes* defined it because *there was no transfer of assets to Wayne County.* Regardless of the Court of Appeals' labeling, *there was no "transfer" of retirement system assets to the County*, either directly or indirectly, because the assets never left the Retirement System. As a result, there was no violation of the prohibited transaction rule.[32]

**c) The Court of Appeals' "prohibited transaction" analysis disregards MCL 38.1140m, which expressly permits a transfer substantially similar to the credit and offset under the 2010 ordinance.**

PERSIA explicitly authorizes the very type of intra-system transfer that the Court of Appeals concluded is prohibited under MCL 38.1133(6)(c). MCL 38.1140m provides that "[i]n a plan year, any current service cost payment may be offset by a credit for amortization of accrued assets, if any, in excess of actuarial accrued liability." MCL 38.1140m thus permits a

[32] For this same reason, Plaintiffs miss the point when they cite inapposite cases rejecting true "transactions" between plans and plan sponsors that are in stark contrast to this case. See, e.g., *Comm'r of Internal Revenue v Keystone Consol Indus, Inc*, 508 US 152; 113 S Ct 2006; 124 L Ed 2d 71 (1993) (employer exchanged certain truck terminals and real property to its defined benefit plan in lieu of satisfying its funding obligation), *Baizer v Comm'r of Internal Revenue*, 204 F3d 1231 (CA 9, 2000) (plan fiduciary transferred accounts receivable to a defined benefit plan in lieu of satisfying the plan's funding obligation), *Peek v Comm'r of Internal Revenue*, 140 TC 12, 2013 US Tax Ct LEXIS 12 (2013) (holding that a loan or loan guarantee between a plan and a disqualified person, even if it goes through a third party proxy, constitutes a prohibited transaction), and *Rollins v Comm'r of Internal Revenue*, TC Memo 2004-260 (Memo Dec 2004) (involving loans from a plan to companies partially owned by a disqualified person)).

system to credit system assets toward an employer's ARC to offset the amount that employer must contribute toward the ARC – just like the offset required by the 2010 ordinance.[33]

In concluding that the 2010 ordinance's credit and offset provision resulted in a "prohibited transaction" under MCL 38.1133(6), the Court of Appeals ignored that MCL 38.1140m expressly permits a nearly identical offset. It should have harmonized the two provisions. The reason the offset provided under MCL 38.1140m is not a "prohibited transaction" under MCL 38.1133(6) is because the retirement system's "assets" remain at all times within the system to pay benefits to system participants, just like the assets transferred from the IEF back into the defined benefit plans under the 2010 ordinance.

## V. CONCLUSION

This Court should reverse the Court of Appeals' published decision and reinstate the Wayne County Circuit Court's decision granting summary disposition to Wayne County.

Respectfully submitted,

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[33] To be clear, Wayne County is not suggesting that MCL 38.1140m authorizes the credit and offset. As already explained, MCL 38.1140m involves "excess" assets in an overfunded defined benefit plan, whereas the 2010 ordinance uses assets held in the separate IEF. However, such a distinction is irrelevant for purposes of harmonizing MCL 38.1140m with MCL 38.1133(6)(c).

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